

**AT&T EXCEPTIONS TO THE ADMINISTRATIVE LAW JUDGE'S
PROPOSED SECOND INTERIM ORDER**

**EXCEPTION 1: THE PROPOSED ORDER INCORRECTLY CONCLUDES THAT
ALL ACCESS LINES SHOULD BE SUPPORTED.**

AT&T provides the following edits to be inserted to the final paragraph on page 4 of the Proposed Order:

The Commission concludes that the list of supported services should be those currently defined by the FCC. Section 13-301(e)(1) (which is made applicable to any inquiry under Section 13-301(d)) provides that the FCC list shall be the minimum list and no party has adduced any convincing evidence that any services should be added. As Ms. Hegstrom noted, the FCC's definition does not specify that services are to necessarily be applied to all access lines or to some subset of access lines. The criteria contained in the federal Telecommunications Act and upon which the FCC relied in its determination includes four components, two of which are key in the Commission's deliberation on this issue: 1) essential to education, public health, or public safety, and 2) have, through the operation of market choices by customers, been subscribed to by a substantial majority of residential customers. (TA96, Section 254(c)) The Commission will apply the definition of universal services to residential access lines only at this time. Parties may revisit this issue in the next Phase of these proceedings if events warrant it. In terms of the primary line/secondary line distinction, as Staff points out, all residence access lines should be supported to prevent rate shock and for administrative simplicity.

Accordingly, AT&T provides the following edits to Ordering Paragraph C of the Proposed Order:

The services defined by the FCC as supported services shall be applied to all residential access lines, and shall be the state supported universal services for purposes of the Fund;

**EXCEPTION NO. 2: THE PROPOSED ORDER INCORRECTLY REJECTS
AT&T'S PROPOSED ADJUSTMENTS TO THE HAI
DEFAULT INPUT VALUES.**

AT&T provides the following edits to be inserted to the Commission Conclusion on page 16 of the Proposed Order:

The Commission has reviewed the cost studies, proposed adjustments and arguments relating thereto and has concluded that the HAI Model, run in the default mode two years ago might have been appropriate, but it, is no longer the most appropriate bench mark to use in establishing the forward looking costs of providing the services subject to potential USF funding. A number of parties have attempted to adjust the Model by changing inputs to more closely resemble the supposedly unique characteristics of particular companies (in the case of Home Telephone and LRTC). However, one of the sponsors of the HAI model, or the oxymoronically unique characteristics of the group (in the case of IITA, MCI, AT&T, and Staff) simply suggests modifications to the input values that would align the results of the HAI 5.0a Model with the results of the updated and more current versions of the HAI Model, the input values of which, as Dr. Clarke testified, have been refined to more accurately reflect the forward-looking economic costs of rural companies as a whole. The Commission is unconvinced that the parties were any more successful at doing so than was the FCC in attempting to do so in its Synthesis Model. The empirical results support this view, given the fact that the results of the IITA's adjusted HAI run resulted in a suggested fund in excess of \$70 million, while the IITA's final request, based upon the ROR examinations of the individual companies came in at approximately \$13 million, a number almost identical to the current DEM weighting fund and HCF combined. As noted by AT&T witness Hegstrom, the HAI model, even when set in the default mode, suggests a fund in the amount of \$303 million. With Mr. Clark's input modifications, the potential fund is reduced to \$12,530,269, a figure much closer to the current level of support the carriers are receiving today. The Commission finds that, because the nature of forward looking costing in the telephone industry assumes diminishing costs, the default settings, along with the modifications suggested by AT&T, in all likelihood capture the long run cost outlook for the small Telcos better than the adjusted cost model initially proffered by the IITA any of the other witnesses.

Accordingly, AT&T provides the following edits to Ordering Paragraph E of the Proposed Order:

The proxy averaged cost of all supported services calculated by running HAI Model 5.0 at default levels, with the input modifications discussed and adopted herein, shall be deemed the economic costs of providing the supported services for purposes of the Fund;

EXCEPTION NO 3: THE PROPOSED ORDER INCORRECTLY REJECTS A COMPANY-BY-COMPANY COST/REVENUE ANALYSIS.

The summary of AT&T's position on this issue as contained in the Proposed Order is inaccurate and misleading. AT&T therefore provides the following summary to be substituted in Section F.3., as found on page 31.

3. AT&T

~~First, AT&T, while not objecting to the use of the HAI results as proffered by IITA,~~ suggests that the HAI results ~~they~~ should be used on an averaged basis, as opposed to an individual company basis. Dr Clarke explains that even the most accurate proxy models will underestimate the costs of some companies while they overestimate the costs of others.

Second, AT&T objects to the use of HAI results as proffered by IITA. Specifically, AT&T contends that IITA approaches the use of this fund much like a revenue pool. The universal service fund under investigation in these proceedings is defined specifically to provide support to companies whose economic costs exceed revenues generated via Commission approved affordable rates for services defined as universal services. The demonstration of need must be company specific. That is, Section 13-301(d) does not allow for a revenue proxy. Ms. Hegstrom asserts that the Commission simply does not have the discretion to order funds to be distributed on any basis that is not consistent with the requirements of Section 13-301(d). AT&T proposes a methodology that employs the average HAI cost model results and compares this with individual company's universal service revenues, individual company's federal support, and individual company's access revenues.

AT&T provides the following edits to be inserted to the Commission Conclusion on page 31 of the Proposed Order:

5. Commission Conclusion on HAI and ROR

The Commission has reviewed the relevant statute, the evidence and the arguments of the parties and has concluded that although none of the exact positions provide either a just or reasonable out come to this inquiry, in the aggregate, We are able to establish a comprehensive method by which a company is deemed eligible for any universal service fund support pursuant to Section 13-301(d) of the PUA. ~~While t~~The Commission was charged with establishing a fund based upon a comparison of the economic costs of providing service to the affordable price of those services. ~~t~~The Commission is un~~convinced that this endeavor necessitated, much less likely resulted in, anything approaching a convincing look at the cost or a proxy of the cost and the actual prices costs of any each of the small companies requesting fund support.~~

Addressing first the issue of examining the costs of the small companies on an individual basis. This is, in the first instance, a matter of statutory interpretation that has not been argued by any of the parties. ~~While~~ Staff's position has been that a "plain reading" of Section 13-301(d) leads to the clear conclusion that individual company analyses are required, ~~our reading of that section, while plain, is not so clear and comports with our reading as well.~~ Section 13-301(d) provides, in pertinent part:

Section 13-301. Consistent with the findings and policy established in paragraph (a) of Section 13-102 and paragraph (a) of Section 13-103, and in order to ensure the attainment of such policies, the Commission shall:

(d) investigate the necessity of and, if appropriate, establish a universal service support fund *from which local exchange telecommunications carriers who pursuant to the Twenty-Seventh Interim Order of the Commission in Docket No. 83-0142 or the orders of the Commission in Docket No. 97-0621 and Docket No. 98-0679 received funding and whose economic costs of providing services for which universal service support may be made available exceed the affordable rate established by the Commission for such services* in establishing any such universal service support fund, the Commission shall, in addition to the determination of costs for supported services, consider and make findings pursuant to paragraphs (1), (2), and (4) of item (e) of this Section. *Proxy cost*, as determined by the Commission, may be used for this purpose.(emphasis added)

We note, however, that although we agree with Staff's interpretation regarding the requirement of individual company analyses, there is nothing to prohibit the use of the average of several individual company costs as a proxy for a specific individual company, or for each company. IITA, as well as other parties, couched every submission relating to the use of cost studies for rural companies with disclaimers as to the reliability if performed on an individual company basis. Thus, the use of the averaged costs of the fifty or so companies mitigates some of the unreliability, and thus the Commission accepts the average costs as an appropriate proxy for the economic costs of the rural companies in question.

Two further matters require comment. Staff has read, and understandably so, this statute ~~as if it~~ to reads ". . . from which a local exchange carrier

who pursuant to the . . . orders of the Commission in Docket No. 97-0621 and Docket No. 98-0679 received funding and whose economic costs of providing services etc.” ~~While understandable,~~ Consistent with this view, our view is that the Statute may not be equally addressed to the entire class of carriers subject to funding under our prior orders, as IITA’s proposal would do, ~~which~~ A view addressing an entire class of carriers would make the inquiry general, rather than specific. Such a view contradicts the very purpose of creating a universal service fund that is operable in an emerging competitive environment. This view is reinforced by the legislature’s singular use of the term singular form “Proxy-cost” in allowing the use of this approach to costing issues only. ~~Had the legislature intended a company-by-company examination, the Commission would have been empowered to use “proxy costs” for each company examined. In fact, the inquiry undertaken here has readily demonstrated the wisdom of the legislature in taking a class wide approach. Every party participating in this docket couched every submission relating to the use of cost studies for rural companies with disclaimers generally found in contracts of adhesion, not testimonial evidence. The evidence is uncontroverted that the FCC had rejected the HAI model as a component of its Synthesis Model and concluded that the production of suitable rural company cost models is well in the future. Nowhere in Section 13-301(d) is there a suggestion or an allowance of the use of a proxy for prices, revenues, or any other factor of the analyses. We therefore reject IITA’s proposal to view the fifty-some company analyses as a whole. In conclusion, support from a Section 13-301(d) fund for any company is limited to the amount by which the economic costs exceeds the prices for universal service, less the level of federal support and less the level of access revenues exceeding access economic costs for each individual company.~~

~~While we are convinced that the use of company specific cost modeling is not required by Statute, we are similarly convinced that even if it were, the asymmetrical application suggested Staff cannot be countenanced. Staff’s proposal would exalt the HAI results in the event they conveniently showed revenue beyond costs but disparage them in the event they showed costs beyond revenue. While Staff attempted to sidestep the issue by referring to the tendency of the HAI to over estimate costs, there was simply no showing that the HAI did so, and in fact, in some cases did the opposite, showing costs under price. The results were simply the results, contrary opinions notwithstanding.~~

Accordingly, AT&T provides the following new Ordering Paragraph of the Proposed Order:

Eligible carriers may receive fund support at a level not higher than the lesser of the HAI analysis and the ROR analysis, as discussed herein;

EXCEPTION NO. 4: THE PROPOSED ORDER INCORRECTLY FAILS TO REDUCE FUND SUPPORT IN THOSE CASES WHERE ACCESS REVENUES ARE CLEARLY SUBSIDIZING UNIVERSAL SERVICES.

AT&T provides the following edits to be inserted to Commission Conclusion section on page 18 of the Proposed Order:

Commission Conclusion

The Commission has reviewed the arguments of the parties and concludes as follows. ~~While the Company specific HAI access charge module suggests that a small number of the small companies may be receiving a subsidy from access charges, the point is immaterial for a number of reasons. First, the Commission has previously decided that the HAI model should be run across all the small companies to determine the proxy cost of providing supported telecommunications services. Similarly, we conclude that the HAI cost results on interexchange access should also be looked at as a whole on an averaged basis, and utilized on a company specific basis. When this is done, the results show that the costs of providing access are greater, across all the companies, less than the revenues being received for some companies, leading to the conclusion that no subsidies are being generated by this revenue stream. For those companies which do not have excess access revenues, yet request universal service fund support, We reject Verizon's recommendation to require these companies to increase their access rates. This investigation was not initiated to determine appropriate access service rates for these companies. Rather, as discussed above, this investigation was initiated to investigate the need for a state universal service fund pursuant to Section 13-301(d) of the PUA. Furthermore, to the extent any company demonstrates its universal service revenues do not exceed economic costs, increasing access revenues to cover these costs creates the implicit subsidies, in direct contradiction to the intent of the statute to eliminate implicit subsidies.~~

For those companies that do have excess access revenues, the record indicates that the excess is not equal to the level of universal services revenue shortfall for these companies. Therefore, we conclude that AT&T's proposal to classify these carriers as ineligible for fund support is too extreme. However, in order to comply with the spirit of the statute, and consistent with our own past policy, we will require any support eventually calculated to be available for any of these companies to be

reduced by the level of excess access revenues in the same manner that support is reduced by the level of federal support. We realize that this methodology does not remove subsidies from the access services, and therefore, does not make the subsidies explicit. Second, even if we were to examine the HAI results on a company by company basis or to be convinced that something were amiss vis-à-vis access charge costs and revenues, the Verizon and AT&T proposals must still fail because the Commission can find no requirement in Section 13-301(e)(2) that would support either. Either proposal would require the Commission to take some action affecting the rates of the small companies, either by ordering access charge rate increases (Verizon's proposal) or an access charge driven USF income reduction (the AT&T proposal). Under Section 13-301(e)(2), however, the Commission is simply charged with, as part of this investigation, the identification of implicit subsidies and the manner in which implicit subsidies may be made explicit. While the Commission has a long history of attempting to reduce or eliminate subsidies in many contexts, there is simply no requirement in Section 13-301(e)(2) that it do so in this proceeding. Accordingly, the proposals of Verizon and AT&T are rejected. The Commission, however, furthermore agrees with IITA that at some time in the near future it may be necessary, whether in an additional phase of this docket, or in a new docket, to examine the impact of federal access reform, through our policy of mirroring for these companies, on the intrastate access charges of the small companies, with an eye to establishing cost based rates, as was recently done in the case of the two largest ILECs in Illinois. At that time We will address how to make any remaining subsidies explicit. This inquiry should, however, not commence, until some sort of certainty concerning small LEC access charges and final USF funding levels are reached at the Federal level, to prevent the sort of running and halting that has affected this docket and other dockets addressing rural company costs being concurrently addressed at the FCC. With this in mind, We note that the HAI studies did suggest that some of the small companies may be receiving access charge revenue in excess of costs and hereby commit to a third phase of this docket that will address, at a minimum, the issue of possible access charge subsidies within those companies and the manner in which the subsidies, if any, may be made explicit. In this way, end users throughout Illinois will not be required to subsidize more than required for Section 13-301(d) universal service purposes, yet companies will continue to be able to receive adequate support for universal services as intended by the statute.

EXCEPTION 5: THE PROPOSED ORDER ARBITRARILY AND DISCRIMINATORILY DETERMINES THAT THE CURRENT RATE IS THE AFFORDABLE RATE.

AT&T provides the following edits to be inserted to Commission Conclusion section beginning on page 28 of the Proposed Order:

Having reviewed the statute, the evidence and the arguments of the parties, the Commission concludes, based upon the record before it, that the affordable rate should be the highest rate assessed within the last ten years of each eligible company at the time the fund is established. In arriving at this conclusion, the Commission notes, first, that such an outcome ~~was specifically contemplated by~~ is consistent with the legislature in its admonishment that any Commission established affordable rate would be no less than the rates in effect at the time a USF fund were established. By utilizing established rates assessed within the last ten years, the Commission has reached a determination within the statutory parameters. ~~To arrive at any other conclusion would have required a much greater evidentiary showing. On this record, the Commission is unconvinced that any of the remaining proposals are adequately supported. As to the establishment of an average affordable rate, the Commission notes that IITA witness Schoonmaker agrees with the concept, albeit not with the various rate levels proposed by Staff and the parties. We hereby adopt Staff's recommendation to establish an average affordable rate for residential service of \$24, exclusive of any federal End User Common Line charges. As Staff as proposed, and we adopt herein, the companies will have the option of increasing their respective residential rates to the affordable rate level. Regardless of whether the residential end user rates are increased, the companies will be required to "impute" the increased rate level in their annual application for funds, thereby concurrently reducing the level of fund support by the level of revenue that would be generated by the allowed increase. Furthermore, the companies are directed to provide to Staff, on an annual basis, the level of increases implemented and the impact on universal services in their respective exchanges. In the next Phase of this docket, but no later than three years from this order, Staff will report to the Commission its analysis, with a recommendation as to whether the \$24 affordable rate level should be revisited. In terms of Staff's proposals, most were based upon an approach of simply doubling recognizable statistical sums (Bureau of Labor Statistics on the one hand and Ameritech Band B and C rates on the other) with no rational explanation why doubling was appropriate. In terms of the additional costs issue, Staff's testimony was internally inconsistent, at times including additional cost considerations while at other time shunning them. There is simply inadequate evidence to support Staff's approach.~~

~~In terms of Verizon's suggestion, the Commission agrees with IITA that Verizon Witness Beauvais apparently miscalculated the usage~~

~~component, which would have reduced the proposed rate from approximately \$23 to \$20, but also failed to take into account the incomparable extended service areas of Verizon and the limited service areas of the eligible companies, making any comparison of the rates suspect from the beginning. In sum, the better approach from both a policy and legal perspective, on this record, is to accept the legislature's invitation to set the affordable rate at the individual rate levels in effect at the time the USF fund is established.~~

~~Given the Commission's decision to apply the definition of universal service to residential access lines only at this time disposition of the affordable rate issue, it is not necessary to address an affordable rate level for business services in these proceedings. the imputation issues raised by Staff, MCI WorldCom and Verizon.~~

Consistent with this exception, the following section should be deleted from page 49.

~~3. Phase In~~

~~While none of the parties were responding to the specific funding proposal adopted in this order, most, is not all, suggested a phase-in process, through which the requesting companies would be allowed to absorb any reductions in the funding levels currently being received from the HCF and DEM Weighting funds. The proposals ranged generally from three to five years although some parties sought immediate and complete first year reductions and others sought to have the first reductions in revenue take place after the end of the first fiscal year of the plan. The Commission concludes that, given the fact that the only reduction ordered to the amount requested by IITA involve the two accounting issues, no phase in is necessary.~~

Accordingly, AT&T provides the following edits to Ordering Paragraph D of the Proposed Order, and adds a new Ordering Paragraph:

The current highest level retail rates of the supported services assessed within the last ten years shall be deemed the "affordable rates" for purposes of the Fund;

The affordable rate of \$24 per month, exclusive of federal Subscriber Line Charges, is hereby adopted for residential access lines. The affordable rate will be implemented pursuant to Staff's proposed five-year transition plan, which is adopted herein;

**EXCEPTION 6: THE PROPOSED ORDER INCORRECTLY AND UNLAWFULLY
ALLOWS A COMPANY TO DRAW STATE FUND SUPPORT FOR
SERVICES THAT ARE NOT UNIVERSAL SERVICES.**

First, in order to make it explicit as an issue, AT&T provides the following edits to be inserted to list of Contested Issues on page 4 of the Proposed Order:

III. CONTESTED ISSUES

As noted above, the parties were unable to reach consensus on all issues. The contested issues include: (1) what services constitute those eligible for support; (2) whether Section 13-301(d) contemplates the use of forward looking costs or embedded costs in establishing the “economic costs of providing services for which universal support may be made available;” (3) whether, in the event a forward looking cost model is used, any adjustment to the inputs of the model are necessary; (4) whether, in the event a forward looking cost model is used, how the results should be used in sizing a universal service fund, (5) whether and how company specific rate of return results should be used in judging the necessity of providing universal service funding to requesting companies; ~~(56)~~ the affordable rate to be used in determining the size or eligibility for USF funds and; ~~(67)~~ whether any USF fund established should be considered the final funding methodology for purposes of triggering the “true up” requirements of previous stipulations and agreements reached by the parties to this docket. In addition, there are a minor number of miscellaneous and company-specific accounting issues that must be decided, as well as an affirmation as to a subsequent phase of this Investigation.

The following summary of AT&T’s position should be appended to the summary on page 31 as amended in Exception 3 above.

AT&T recommends a methodology in which the fund support for any rural LEC is capped at the smaller amount resulting from a ROR analysis and an HAI analysis. Without these adjustments, Ms. Hegstrom explains, if a company were not in an over-earnings situation as a result of the embedded cost ROR analysis, the company would be eligible to receive the total revenue shortfall created by comparing an affordable rate to the economic cost proxy. In some cases, this would provide an amount of fund support that would put a company into an over-earnings situation. In other words, in this situation, the fund would create and support over-earnings of a company even though the overlay of the ROR analysis is intended to prevent this very thing. Similarly, if the HAI analysis revenue shortfall were less than the ROR analysis revenue shortfall, distributing

funds equal to the ROR analysis revenue shortfall would result in the fund providing support for services beyond those included in the definition of universal services.

AT&T further provides the following edits to be inserted to the Commission Conclusion section, beginning with the first full paragraph on page 33 of the Proposed Order:

We turn now to the ROR results. Staff notes correctly that the Commission was vitally interested in gaining some perspective on the current earnings positions of the companies now before us seeking funding. That was provided in the ROR results. The question now becomes what to make of them given our previous decision that the individual company HAI results ~~should not~~ must be used as a tempering medium. We have reviewed the results and note that ~~they indicate rates of return ranging from 9.99% on the high side to 36.19% on the low side. The raw figures provide more questions than they do answers. To find that a company is earning around 10% and surviving is not too surprising, to find that a company is earning 36% and surviving is quite surprising. The bottom line is that none of the parties appear to be in an over-earning position vis-à-vis basic services, on an overall basis, which was the essential nature of our inquiry, several companies appear to be in an over-earnings position. This would indicate to the Commission that, even if the economic costs of universal service exceeded these companies' prices for universal service, revenues are currently being generated elsewhere sufficient to provide the subsidy needed for universal services. Thus, we agree with Staff and parties that any company in an over-earnings position should not be eligible for universal service fund support.~~

Although the ROR results have provided us with some degree of comfort in terms of the earnings levels of other ~~the~~ requesting companies, that comfort is disturbed somewhat by the prospect of using the results as requested by IITA; as the undisturbed baseline for setting the size of the fund. Many of the parties to this proceeding have argued that the USF fund was not meant to be a "keep whole" fund, which, they assert, is what would result from simply setting funding levels that would allow each company to maintain its current ROR. The argument is facially appealing, yet flawed. ~~Two matters bear comment. First, w~~While the legislature has spoken directly to the issue of maintaining the affordability of universal service to end users, it was silent concerning the potential impact on the companies before us in this docket. Thus, there is no legislative ~~prohibition against taking steps~~ requirement to insure that the small companies rates of return are not negatively impacted by the institution of a USF fund, ~~especially here, where we have been provided with record evidence that none of the companies are in an over-earnings situation given the knowledge that any company in this position has other~~

regulatory opportunities to correct or mitigate the situation. Furthermore, as discussed above, we are herein adopting a process to price residential access lines at an affordable rate, to which these companies may avail themselves regardless of their current eligibility status to receive universal service fund support.

~~Further, the Commission agrees with AT&T that it would be inconsistent with the intent of the statute if, as a result of a company receiving Section 13-301(d) support, a company would enter into an over-earnings position. Therefore, eligible companies as defined above, are limited to receiving support at the lesser of the HAI analysis amount and the ROR analysis amount. an examination of the entire statutory scheme of section 13-301 indicates that the legislature may well have intended that the USF established under Section 13-301(d) maintain the small companies at status quo. Section 13-301(d) requires the Commission to perform four tasks in establishing a USF. First, identify those services to be declared supported telecommunications services. Second, establish an affordable rate for those services. Third, determine whether the small companies economic costs of providing those services exceed the affordable rate. Fourth, identify any implicit subsidies and determine how those subsidies may be made explicit. Of these four tasks, three (the first, second and fourth) are all imported into section 13-301(d) from section 13-301(e). Of particular note is that at no point did the legislature suggest that the rates of the small companies should be subject to modification. This is strikingly different than the approach taken to the inquiry under Section 13-301(e), where receipt of USF funds is specifically triggered by the identification and elimination of existing implicit subsidies "through revisions to rates or charges." The Commission finds that the absence of any reference to revisions to rates or charges to the inquiry under Section 13-301(d) suggests that the legislature was keenly interested in maintaining the status quo for the companies before us here and the customers of those companies. To that end, we conclude that, as suggested by the IITA, the ROR analyses should form the baseline for establishing the USF fund. In addition to simplifying the process of establishing the fund at the outset, this process also moots the necessity of further engaging the scarce resources of the companies and the Commission in engaging in Staff's ill-defined informal dispute resolution process, through which an aggrieved company could supplicate itself before staff in an effort to rescind the reduction in USF funding by demonstrating that the ROR study was more real than the HAI model run. Such a procedure is rife with due process issues that were not explained or explored in the record before us and that should be avoided if at all possible.~~

Given fact that We have adopted the ROR analyses as ~~the baseline a~~ tempering medium for the USF fund size, the next matter that requires additional discussion are a number accounting adjustments to specific company ROR's proposed by Staff.

Consistent with this exception, AT&T provides the following edits to the Commission Conclusion contained on page 45.

~~The Commission has reviewed the evidence and arguments of the parties and has reached the following conclusions. The Staff adjustment to the ROR showing of MITCO is accepted. The Staff adjustment to the Frontier companies is not accepted. The Staff adjustment to Gridley is accepted. We explain these conclusions below. Before turning to our discussion of each particular case a general observation is warranted. In these dockets, the Commission had requested and received from each small company, a truncated rate of return showing. As noted previously, that rate of return review was intended, in the first instance, to allow the Commission to conclude that, based upon the limited review necessitated by the short time frame associated with these dockets, that none of the small companies were in an over-earnings situation. Our review of the submission indicates that none are. We then adopted the ROR analyses as the benchmark against which to measure the potential size of the fund. To that end, Staff reviewed the submission and, as has been the practice in the past, suggested adjustments to the proposals similar to those that would have been made had the various companies come in for rate cases. While understandable, We can find no explicit requirement that rate of return adjustments, such as those contemplated under Article IX of the PUA would necessarily apply to the establishment of a USF. Rather, it would seem that the wide discretion vested the Commission under Section 13-301(d) contemplates adjustments to the size of the fund based upon the needs of the carriers, as shown by the ROR results. To that end, the acceptance of any adjustment in this Order will have no effect, and should not be cited as precedent in any ratemaking proceeding under Article IX of the PUA. The Commission further agrees with Verizon and other parties that any changes the carriers experience in their federal support must also be reflected in the HAI/ROR analyses.~~

~~Turning now to the actual adjustments. In terms of MITCO, the Commission~~

AT&T further provides the following edits to Ordering Paragraph E of the Proposed Order:

An initial Universal Service Fund in the amount of ~~\$12,959,292~~ \$12,959,292.5,875,087, less the adjustments necessary to give effect to the two Staff accounting

adjustments discussed in Section G. 5 above, adjusted by any changes to the carriers' federal support, plus administrative expenses, is hereby established pursuant to Section 13-301(d) of the Illinois Public Utilities Act;

EXCEPTION 7: THE PROPOSED ORDER SHOULD RESOLVE THE DEM WEIGHTING ISSUES BY ADOPTING THE COMPETITIVELY NEUTRAL FUNDING METHOD ORDERED IN THIS PHASE AS THE PERMANENT FUNDING METHOD FOR PURPOSES OF ACCOMPLISHING THE AGREED UPON TRUE UP OF THE DEM WEIGHTING FUND.

AT&T provides the following edits to be inserted to the Miscellaneous Issues on page 48 of the Proposed Order:

1. True up of HCF and DEMem Weighting Funds

~~The Commission's First Interim Order thoroughly discussed the genesis and history of the HCF and DEM weighting Funds. The Order also concluded that the issue was not ripe for decision and put off any final decision until such time as a final funding methodology was in place. While ~~this~~ This Order establishes a final funding methodology, thus making it appropriate that We make a final determination as to the methodology for implementing any true-ups to the DEM Weighting Funds established pursuant to Docket Nos. 97-0621 and 98-0679. ~~considerations of administrative efficiency and the fact that We have previously committed to at least one more phase of these dockets, convince us that this determination should again be deferred. The record and issues to be considered here are voluminous and complex. The time frame for resolution is short. The issue of the final funding methodology and any possible true up is also complex, but is not as time sensitive, given the fact that any true up that may be ordered, will have no effect until such time as a final funding methodology is established. Accordingly, the Commission will take up HCF and DEM Weighting true up issues in the next phase of these dockets. It is anticipated that these issues, which have already been briefed, will be the subject of an additional interim order shortly following the expiration of the rehearing period and/of any rehearing granted following the entry of this order.~~~~

The DEM Weighting Order clearly contemplated true-ups to the sums paid into the DEM Weighting fund over the course of its existence. We note with particularity Verizon's continuous and staunch opposition to the inclusion of any true-up requirement, from which we infer that at least some of the parties to that docket were aware that a sea change in the

manner of funding was possible. It is also recognized that parties anticipating a refund have been since the expiration of the initial DEM Weighting Fund in 1998.

In these proceedings, Verizon relies heavily on our determination of the DEM Weighting Funds as access revenue replacement funds. Verizon fails to accept the fact that any true-up to the establishment of a permanent funding mechanism. That has been done in this Second Interim Order.

This Order establishes a final funding methodology, basing assessments on intrastate retail revenues less both uncollectible expense and revenues received from any end use surcharge imposed as a result of this Order, and we hereby adopt it as the Permanent Funding Method by which the true-ups specified in the Stipulated Agreements we approved in ICC Docket Nos. 97-0621 and 98-0679 shall be accomplished. To that end, we hereby appoint the ISCECA as the Funding Administrator for purposes of administering the true-ups, and direct ISCECA to administer, implement and finalize the true-ups (subject to the cap) within 60 days of our entry of this Order.

Accordingly, AT&T provides the following new Ordering Paragraphs of the Proposed Order:

The funding methodology we adopt for the Section 13-301(d) Fund shall constitute the Permanent Funding Methodology for purposes accomplishing and administering the true-up of the DEM Weighting Fund from 1998 through the expiration of the present fund;

The ISCECA shall complete the true-up of the DEM Weighting Fund from 1998 through September 30, 2001 within 60 days of the entry of this Order;

EXCEPTION NO. 8: THE PROPOSED ORDER SHOULD ENUMERATE THE ISSUES TO BE ADDRESSED IN THE NEXT PHASE

AT&T provides the following language to be added as the last Miscellaneous Issues on page 49 of the Proposed Order:

4. Issues To Be Addressed In Phase III

Several of the parties have raised issues that we feel should be addressed in the next phase of this proceeding. We hereby establish Phase III of this proceeding, and direct that the following issues shall be addressed and resolved in Phase III, at a minimum: (1) a mechanism to

transition the state universal service fund we establish herein pursuant to Section 13-301(d) to a Section 13-301(e) fund; (2) the possibility of designing a funding mechanism whereby universal service support is provided directly to the end user rather than to the ILEC; and (3) has any access charge subsidies may be made explicit.

Accordingly, AT&T provides the following addition to the Ordering Paragraphs of the Proposed Order:

A third phase to this investigation will be initiated no sooner than the release of an FCC Order adopting access charge reform for non-price cap carriers, and no later than two years from the entry of this Interim Order. Staff shall prepare a list of issues to be addressed in the third phase of this investigation, including at a minimum those described above;

AT&T summarizes the inclusion of its exceptions into the Ordering Paragraphs as follows:

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that:

- A. An initial Universal Service Fund in the amount of ~~\$12,959,292~~ 5,875,087, less the adjustments necessary to give effect to the two Staff accounting adjustments discussed in Section G. 5 above, plus administrative expenses, is hereby established pursuant to Section 13-301(d) of the Illinois Public Utilities Act;
- B. The Fund shall become effective October 1, 2001 and shall remain in effect until dissolved by order of the Commission. Concurrent with the establishment of this Fund, the Illinois High Cost Fund established pursuant to the Twenty-Seventh Interim Order in ICC Docket No. 83-0142 is dissolved;
- C. The services defined by the FCC as supported services shall be applied to all residential access lines, and shall be the state supported universal services for purposes of the Fund;
- D. Eligible carriers may receive fund support at a level not higher than the lesser of the HAI analysis and the ROR analysis, as discussed herein;
- ~~DE.~~ The ~~current~~ highest level retail rates of the supported services assessed within the last ten years shall be deemed the "affordable rates" for purposes of the Fund;

- F. The affordable rate of \$24 per month, exclusive of federal Subscriber Line Charges, is hereby adopted for residential access lines. The affordable rate will be implemented pursuant to Staff's proposed five-year transition plan, as is described herein;
- EG. The proxy averaged cost of all supported services calculated by running HAI Model 5.0 at default levels, with the exception of the modifications discussed herein, shall be deemed the economic costs of providing the supported services for purposes of the Fund;
- FH. All local exchange carriers and interexchange carriers certificated in Illinois shall contribute to the Fund on the basis of their intrastate retail revenues, consistent with Section 13-301(d) of the PUA and the Agreement submitted by the parties to this case, which is hereby approved and incorporated into this Order;
- GI. All carriers contributing to the Fund shall timely provide to the Fund Administrator and Staff, in the first instance, all information necessary to determine each carrier's intrastate net retail revenues;
- HJ. All carriers contributing to the Fund shall recover their fund contributions from their end user customers via an explicit end user surcharge on the customer's bill. The surcharge shall be assessed in a competitively neutral manner consistent with existing Illinois rules and statutes;
- IK. All carriers contributing to the Fund shall be prohibited from recovering their funding commitments from another certificated carrier for any service purchased and used solely as an input to a service provided to such certificated carrier's retail customers;
- JL. The ISCECA is appointed as the Fund Administrator of the Fund;
- M. The funding methodology we adopt for the Section 13-301(d) Fund shall constitute the Permanent Funding Methodology for purposes of accomplishing and administering the true-up of the DEM Weighting Fund from 1998 through the expiration of the present fund;
- N. The ISCECA shall complete the true-up of the DEM Weighting Fund from 1998 through September 30, 2001 within 60 days of the entry of this Order;

- O. A third phase to this investigation will be initiated following the release of an FCC Order adopting access charge reform for non-price cap carriers, but no later than two years from the entry of this Interim Order. Staff shall prepare a list of issues to be addressed in the third phase of this investigation, including at a minimum those issues described above;